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8 UNITED STATES DISTRICT COURT
9 NORTHERN DISTRICT OF CALIFORNIA
10

11 WELLS FARGO ADVISORS, LLC, a
12 limited liability company,
13 Petitioner,
14 vs.
15 KENNETH C. SHAFFER, an individual,
16 Respondent.
17 _____/

18 AND RELATED COUNTERCLAIMS
19
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Case No. CV-01500 SC

**MEMORANDUM OF POINTS AND
AUTHORITIES IN OPPOSITION TO
WELLS FARGO ADVISORS, LLC'S
MOTION TO VACATE ARBITRATION
AWARD**

DATE: June 10, 2011
TIME: 10:00 a.m.
COURTROOM: 1, 17th Floor

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I. INTRODUCTION

Wells Fargo Advisors, LLC (“WFA”)’s petition is an unwarranted attempt to re-litigate the facts of an arbitration proceeding which its predecessor, Wells Fargo Investments, LLC (“WFI”) lost, after a full and fair trial on the merits. Specifically, an arbitration panel of the Financial Industry Regulatory Authority (“FINRA”), applying controlling precedent from the California Supreme Court, ruled that the promissory note WFI sought to enforce against respondent Kenneth C. Shaffer was unenforceable because it was unconscionable. (Exh. 6.) The FINRA arbitration panel further ruled that Mr. Shaffer was entitled to recover damages in the amount of \$75,000 from WFI, because of the defamatory statements it made on his Form U-5.¹ (Exh. 6.) California law is clear that both of the foregoing determinations that were made by the arbitrators in Mr. Shaffer’s case are fact questions, which could not have been made as a matter of law. Such factual determinations are plainly outside the limited scope of permissible judicial review of arbitration awards.

Nonetheless, WFA insists that the arbitration award must be overturned for alleged “manifest disregard of the law”. WFA’s argument ignores the meaning of this term, and the very narrow circumstances in which it applies. Contrary to WFA’s assertions, “manifest disregard of the law” does not mean that an arbitration award is subject to vacatur merely because the arbitrators disagreed with WFA’s characterization of the facts and evidence, or interpreted and applied case law differently than WFA thinks they should have. Instead, WFA has the burden of proving that the arbitrators specifically recognized and correctly stated controlling law, and then proceeded to ignore that same law. WFA has utterly failed to meet that burden for three reasons.

First, the decisions made by the arbitrators were factual determinations which could not have been made as a matter of law. Secondly, the case law relied upon by WFA is neither controlling nor applicable. Third, even if the cases cited by WFA were controlling - and they are not - there

¹ A Form U-5 is a standardized form that broker-dealers are required to submit to FINRA whenever a registered representative’s registration with that broker-dealer has terminated for any reason, voluntary or involuntary. (Exh. 7; *Baravati v. Josephthal, Lyon & Ross, Inc.* 28 F.3d 704, 705, 708 (7th Cir. 1994).)

1 would still not be any manifest disregard of the law, as defined by the Ninth Circuit, because the
 2 arbitrators did not cite to any of those cases in their award, nor at any other time during the
 3 proceeding.

4 Indeed, WFA has failed to provide one iota of evidence that there was “manifest
 5 disregard of the law” under the standards set forth by the Ninth Circuit. The exact opposite is
 6 true. The arbitration award recognized, correctly stated, and applied controlling precedent from
 7 the California Supreme Court.

8 WFA should not be allowed to use this petition as a back door way to re-try the merits of
 9 a case which WFI tried and lost in arbitration. This honorable court should deny WFA’s petition
 10 to vacate the award, and award Mr. Shaffer the attorneys fees he has been forced to incur as a
 11 result of having to oppose this petition.

12 **II. ISSUES TO BE DECIDED**

13 1. Has WFA proven the existence of any of the circumstances for vacating an arbitration
 14 award that are set forth in Section 10 of the Federal Arbitration Act?

15 2. Should Mr. Shaffer be awarded his attorneys fees incurred in opposing this motion,
 16 pursuant to the promissory note with WFI?

17 **III. PROCEDURAL HISTORY**

18 Respondent Kenneth C. Shaffer signed a promissory note with Wells Fargo Investments,
 19 LLC (“WFI”), the predecessor company to petitioner Wells Fargo Advisors, LLC (“WFA”), in
 20 January of 2008. (Exh. 1.) In that note, WFI inserted an arbitration provision which provided
 21 that any controversy regarding the validity, enforcement, or construction of this Note, or any
 22 dispute concerning Mr. Shaffer’s employment or termination of employment with WFI, shall be
 23 resolved by binding arbitration under the rules of the National Association of Securities Dealers
 24 (now known as FINRA²). (Exh. 1 p. 2.)

25
 26
 27 ² The National Association of Securities Dealers changed its name to the Financial Industry Regulatory
 28 Authority (“FINRA”) in 2007, when it merged with the regulatory arm of the New York Stock Exchange.

1 In February of 2010, WFI filed a Statement of Claim with FINRA Dispute Resolution.
2 (Exh. 2.) WFI alleged that it was entitled to recover \$74,617.76 plus interest and attorneys fees
3 pursuant to the terms of the promissory note. (Exh. 2.) WFI also executed and submitted a
4 FINRA Arbitration Submission Agreement by which it submitted the matter in controversy,
5 including the allegations set forth in the Statement of Claim, as well as all answers and all related
6 cross claims, counterclaims and/or third party claims, to binding arbitration in accordance with
7 the FINRA By-Laws, Rules and Code of Arbitration Procedure. (Exh. 3.) WFI expressly agreed
8 to be bound by FINRA's rules and procedures. (Exh. 3.) WFI further agreed to abide by and
9 perform any award(s) rendered by the arbitration panel. (Exh. 3.)

10 In April, 2010, Mr. Shaffer submitted an Answer to WFI's Statement of Claim and a
11 FINRA Arbitration Submission Agreement. (Exh. 4.) In May of 2010, Mr. Shaffer submitted a
12 Counter-claim in the Arbitration. (Exh. 5.) This Counter-claim was submitted on a FINRA
13 Claim Information Sheet form, which is available on FINRA's web-site. (Exh. 5; Decl. of
14 Kenneth C. Shaffer ¶ 6.) This form lists the types of disputes and claims which FINRA hears
15 and decides, with boxes to be checked for the applicable claims. Mr. Shaffer checked the boxes
16 for "Commissions", "Discrimination Disability", "Libel or Slander on Form U-5", "Promissory
17 Notes", "Wrongful Termination" and "Defamation" on this form. (Exh. 5.) On or about May
18 25, 2010, WFI filed a response to Mr. Shaffer's counterclaims. (Shaffer Decl. ¶ 7.)

19 A two day evidentiary hearing was held in San Francisco, California, before a FINRA
20 arbitration panel on January 4, 2011 and January 5, 2011. (Exh. 6.) The arbitrators were Thomas
21 D. Reese, Laurel Littman Gothelf, and Marlyn G. McClaskey. (Exh. 6.) WFI was represented
22 by Ronald P. Kane, Esq. of Kane & Fisher, Ltd. (Exh. 6.) Mr. Shaffer appeared in pro per.
23 (Exh. 6.) He could not afford to retain an attorney to represent him. (Shaffer Decl. ¶ 8.) The
24 panel heard extensive testimony from Mr. Shaffer, and from employees and agents of WFI.
25 (Shaffer Decl. ¶ 8.) Numerous documents were received into evidence. (Shaffer Decl. ¶ 8.)

26 On January 18, 2011, the arbitrators issued their award. (Exh. 6.) The Panel denied
27 WFI's claims against Mr. Shaffer in their entirety. (Exh. 6.) The panel ruled that WFI shall pay
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1 compensatory damages in the amount of \$75,000.00 to Mr. Shaffer. (Exh. 6.) The panel further
 2 recommended that the Termination Comment in Mr. Shaffer's Form U-5 be expunged and
 3 replaced with other language, as set forth in the award. (Exh. 6.)

4 **IV. LEGAL STANDARD FOR VACATING AN ARBITRATION AWARD.**

5 Section 10 of the Federal Arbitration Act ("FAA") sets forth very limited grounds for
 6 vacating an arbitration award. A district court is permitted to vacate an arbitration award only
 7 under one of the following four circumstances:

- 8 1) where the award was procured by corruption, fraud or undue means;
- 9 2) where there was evident partiality or corruption in the arbitrators, or either of them;
- 10 3) where the arbitrators were guilty of misconduct in refusing to postpone the hearing,
 11 upon sufficient cause shown, or in refusing to hear evidence pertinent and material to the
 12 controversy; or of any other misbehavior by which the rights of any party have been prejudiced;
 13 or
- 14 4) where the arbitrators exceeded their powers, or so imperfectly executed them that a
 15 mutual, final, and definite award upon the subject matter submitted was not made. (9 USC § 10.)

16 The grounds set forth in Section 10 of the FAA, stated above, are the exclusive grounds
 17 for vacating an arbitration award under the FAA. (*Hall Street Associates LLC v. Mattel, Inc.* 552
 18 U.S. 576, 584 (2008).) Neither the federal courts, nor the parties, are authorized to expand
 19 judicial review of an arbitration award beyond the specific statutory grounds enumerated in
 20 Section 10 of the FAA. (*Id.* at 585-588.) As the United States Supreme Court explained, any
 21 other conclusion would open the door to full-bore legal and evidentiary appeals, which would
 22 defeat the purpose of arbitration as an informal, expeditious and affordable means of resolving
 23 disputes. (*Id.* at 588.)

24 The standard for vacatur under Section 10(4) of the FAA is high. (*Lagstein v. Certain*
 25 *Underwriters at Lloyd's London* 607 F.3d 634, 641 (9th Cir. 2010).) It is not enough to show
 26 that the arbitrators committed an error of law or fact - or even a serious error. (*Id.*) Arbitrators
 27 do not exceed their powers under Section 10 of the FAA merely by misinterpreting the law,
 28

1 failing to apply the law, and/or by applying the law incorrectly. (*Id.*) On the contrary, neither
 2 erroneous legal conclusions nor unsubstantiated factual findings justify vacatur of an arbitration
 3 award under the FAA. (*Bosack v. Soward* 586 F.3d 1096, 1102, 1104 (9th Cir. 2009); *Kyocera*
 4 *Corporation v. Prudential-Bache T Services, Inc.* 341 F.3d 987, 994 (9th Cir. 2003).) Indeed, a
 5 district court is **PROHIBITED** from reviewing the arbitrators' factual findings and legal
 6 conclusions. (*Bosack, supra*, 586 F.3d at 1104, emphasis added; *Kyocera, supra*, 341 F.3d at
 7 994.)

8 Similarly, a claim that the arbitrators' conclusions are not supported by the evidence in
 9 the record is beyond the scope of a federal court's review. (*Lagstein, supra*, 607 F.3d at 641;
 10 *Bosack, supra*, 586 F.3d at 1105.) The district court has no authority to re-weigh the evidence
 11 presented to the arbitration panel. (*Bosack, supra*, 586 F.3d at 1105; *Coutee v. Barington*
 12 *Capital Group L.P.* 336 F.3d 1128, 1134 (9th Cir. 2003).)

13 **V. THE ARBITRATORS DID NOT MANIFESTLY DISREGARD THE LAW.**

14 **A. The Arbitrators' Decisions Were Factual Determinations Which Are Not** 15 **Subject to Judicial Review under the FAA.**

16 A district court does not have the power under the FAA to reverse the factual findings
 17 made by the arbitrators. (*Lagstein, supra*, 607 F.3d at 640-641; *Carter v. Health Net of*
 18 *California* 374 F.3d 830, 838 (9th Cir. 2004).) Similarly, an arbitrator's interpretation of a
 19 contract is not subject to judicial review, and is not a valid grounds for vacating an arbitration
 20 award. (*Lagstein, supra*, 607 F.3d at 642.) As the Ninth Circuit has explained, "manifest
 21 disregard of the facts is not an independent ground for vacatur in this circuit." (*Coutee, supra*,
 22 336 F.3d at 1133.)

23 Here, while WFA contends that the arbitrators were wrong as a matter of law, in reality,
 24 WFA is seeking judicial review of the arbitrators' factual findings. Contrary to WFA's
 25 assertions, there is no California legal precedent which militated the arbitrators to rule in WFI's
 26 favor as to either the enforceability of the note or Mr. Shaffer's claims regarding the defamatory
 27 statements on his Form U-5. The exact opposite is true. The California Supreme Court has
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1 unequivocally held that the resolution of both issues is a fact question which depends upon the
 2 weighing of evidence and the resolution of disputed factual issues. Such factual determinations
 3 are not subject to judicial review under the FAA. (*Lagstein, supra*, 607 F.3d at 642; *Bosack,*
 4 *supra*, 586 F.3d at 1102, 1104-1105; *Carter, supra*, 374 F.3d at 838; *Kyocera, supra*, 341 F.3d at
 5 994; *Coutee, supra*, 336 F.3d at 1133-1134.)

6 **1. The Unconscionability of the Note Is a Factual Determination**

7 The arbitrators ruled that the promissory note WFI sought to enforce was procedurally
 8 and substantively unconscionable under the standards set forth in *Armendariz v. Foundation*
 9 *Health Psychcare Services, Inc.* (2000) 24 Cal.4th 83. (Exh. 6.) In *Armendariz*, the California
 10 Supreme Court held that an arbitration agreement in a contract that an employee was induced to
 11 sign as a condition of employment was procedurally and substantively unconscionable. The
 12 *Armendariz* court based its ruling upon its interpretation of the terms of the agreement, the
 13 relationship between the employer and the employee, and the circumstances under which the
 14 agreement was made. (*Id.* at 114-115, 120-121.) It is plainly apparent from the *Armendariz*
 15 opinion that the question of whether a particular contract or term contained therein is
 16 unconscionable is a case-specific factual determination which depends upon the terms and
 17 language of that particular contract, the parties' relationship, and the circumstances under which
 18 that contract was made.

19 Indeed, the California courts have consistently held that the determination of whether a
 20 particular instrument is unconscionable requires the trier of fact to both interpret the parties'
 21 contract and to resolve numerous factual issues which go beyond merely examining the face of
 22 the contract. (*Perdue v. Crocker Nat'l Bank* 38 Cal.3d 913, 926 (1985); *Independent*
 23 *Association of Mailbox Center Owners v. Superior Court* 133 Cal. App.4th 396, 407; *Gutierrez*
 24 *v. Autowest, Inc.* 114 Cal. App.4th 77, 89 (2003); *Bolter v. Superior Court* 87 Cal. App.4th 900,
 25 907 (2001.) For example, before deciding the issue of unconscionability, the trier of fact must
 26 hear evidence regarding the commercial setting, purpose and effect of the contract. (C.C.P. §
 27 1670.5(b); *Perdue, supra*, 38 Cal.3d at 926; *Independent Association of Mailbox Center Owners,*
 28

1 *supra*, 133 Cal. App.4th at 407 2005); *Bolter, supra*, 87 Cal. App.4th at 907.) As the California
 2 courts recognize, the determination as to whether a particular instrument is unconscionable is
 3 dependent upon the unique facts and evidence of each particular case.

4 The intensively factual nature of unconscionability is borne out by WFA's own
 5 arguments, which are devoted to re-arguing the facts. Specifically, WFA claims that the note
 6 was voluntary, that it was not imposed upon Mr. Shaffer, that nothing in it was a surprise to Mr.
 7 Shaffer, and that the note was not one-sided nor overly harsh. (Motion to Vacate pp. 9-13.)
 8 WFA's arguments are nothing more than disagreements with the arbitrators' interpretation of the
 9 promissory note, and the arbitrators' factual and evidentiary findings regarding the commercial
 10 setting, purpose and effect of the note, the relationship between the parties, and the circumstances
 11 under which the note was made. WFA's assertion that such disagreements warrants vacatur is
 12 plainly improper.

13 As the Ninth Circuit has repeatedly stated, "neither erroneous legal conclusions nor
 14 unsubstantiated factual findings justify federal court review of an arbitration award under the
 15 FAA, which is unambiguous in this regard." (*Bosack, supra*, 586 F.3d at 1102, 1104; *Kyocera,*
 16 *supra*, 341 F.3d at 994.) A district court does not have the power under the FAA to re-weigh the
 17 evidence presented to the arbitrators nor to reverse the factual findings made by the arbitrators
 18 after a full and fair trial on the merits, merely because the losing party disagrees with them.
 19 (*Lagstein, supra*, 607 F.3d at 640-641; *Bosack, supra*, 586 F.3d at 1105; *Carter, supra*, 374 F.3d
 20 at 838; *Coutee, supra*, 336 F.3d at 1133-1134.) Indeed, as the United States Supreme Court
 21 explained, allowing such an attack on an arbitration award would defeat the very purpose of
 22 arbitration. (*Hall Street, supra*, 552 U.S. at 588.)

23 **2. Mr. Shaffer's Right to Recover Damages for the Statements Made in**
 24 **His Form U-5 Is a Fact Question That the Arbitrators Had the Right**
and Obligation to Decide.

25 WFA also contends that the arbitration panel manifestly disregarded the law in awarding
 26 Mr. Shaffer damages for the statements WFI made on his Form U-5. Specifically, WFA argues
 27 that every statement on every Form U-5 is subject to an absolute privilege and can never be the
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1 basis of a lawsuit, no matter what the circumstances. That is not a correct statement of the law.
 2 Pre-litigation communications such as statements on a Form U-5 are only subject to an absolute
 3 privilege if they relate to litigation that is contemplated in good faith and under serious
 4 consideration. The California Supreme Court holds that this determination is a fact question.
 5 The FINRA arbitration panel could not have manifestly disregarded the law by making a factual
 6 determination that the Form U-5 was not absolutely privileged.

7 The litigation privilege of California Civil Code section 47(b) bars any action that is
 8 based upon a statement made in any 1) legislative proceeding, 2) judicial proceeding, 3) in any
 9 other official proceeding authorized by law, or 4) in the initiation or course of any other
 10 proceeding authorized by law and reviewable pursuant to C.C.P. § 1084 et. seq. (C.C. § 47(b).)

11 A pre-litigation communication is only protected by the absolute privilege of Section
 12 47(b) if it relates to litigation that is contemplated in good faith and under serious consideration.
 13 (*Action Apartment Association, Inc. v. City of Santa Monica* 41 Cal.4th 1232, 1251 (2007).)
 14 Whether a pre-litigation communication relates to litigation that is contemplated in good faith
 15 and under serious consideration is an issue of fact. (*Id.*)

16 In *Action Apartment, supra*, the California Supreme Court held that, because a factual
 17 inquiry is required in order to determine whether a particular pre-litigation communication is
 18 privileged, it is impossible to conclude that the litigation privilege would bar every action based
 19 upon such a communication as a matter of law. (*Id.* at 1252, emphasis added.) The California
 20 Supreme Court concluded that the trial court's decision granting summary judgment based upon
 21 the litigation privilege must be reversed, since that decision could not be made as a matter of law.
 22 (*Id.*)

23 The foregoing holding applies with equal force here. Mr. Shaffer's Form U-5 was not a
 24 pleading that was submitted in the course of litigation, nor in any other "official proceeding", nor
 25 in any proceeding that is reviewable pursuant to C.C.P. § 1084 et. seq. A Form U-5 is neither a
 26 complaint nor a lawsuit. A Form U-5 is simply a standardized form that all broker-dealers are
 27 required to submit to FINRA whenever a registered representative's registration with a broker-
 28

1 dealer has terminated for any reason, voluntary or involuntary. (see Exh. 7; *Baravati v.*
 2 *Josephthal, Lyon & Ross, Inc.* 28 F.3d 704, 705, 708 (7th Cir. 1994).) Further, FINRA is not a
 3 governmental agency. It is a privately held Delaware corporation which serves as a non-
 4 governmental regulator for securities firms. (Exhs. 8 & 9.)

5 Consequently, under California law, Mr. Shaffer's claims that were based upon the Form
 6 U-5 could only be barred by the litigation privilege if the Form U-5 related to litigation that was
 7 contemplated in good faith and under serious consideration. As discussed above, the California
 8 Supreme Court has ruled that this is a factual determination that cannot be made as a matter of
 9 law. (*Action Apartment, supra*, 41 Cal.4th at 1251-1252.) Such factual determinations are
 10 exclusively within the province of the arbitrators, and are not subject to judicial review. (*Bosack,*
 11 *supra*, 586 F.3d at 1102, 1104; *Carter, supra*, 374 F.3d at 838; *Kyocera, supra*, 341 F.3d at 994;
 12 *Coutee, supra*, 336 F.3d at 1133.)

13 **B. The Law Relied upon by WFA Is Not Controlling Nor Clearly Applicable**
 14 **Precedent.**

15 Despite the holdings from the California Supreme Court, discussed above, WFA argues
 16 that the arbitrators were absolutely required to rule in WFI's favor on all issues, as a matter of
 17 law. Specifically, WFA contends that three cases which WFI provided to the arbitrators³ were
 18 dispositive as to all issues, regardless of the facts. In reality, the cases cited by WFA are not the
 19 conclusive authority that WFA claims them to be, as discussed in detail below. The arbitrators
 20 did not manifestly disregard the law, simply because they properly concluded that the authorities
 21 cited by WFI were inapplicable and/or were not binding precedent.

22 In order to show manifest disregard of the law, the governing law alleged to have been
 23 ignored by the arbitrators must be *well defined, explicit and clearly applicable*. (*Collins v. D.R.*
 24 *Horton, Inc.* 505 F.3d 874, 879 (9th Cir. 2007), emphasis in original; *Carter, supra*, 374 F.3d

25 ³ Those cases are *Federal Savings and Loan Insurance Corp. v. Musacchio* 695 F. Supp. 1044 (N.D. Cal.
 26 1988), *Koehl v. Verio, Inc.* 142 Cal. App.4th 1313 (2006) and *Fontani v. Wells Fargo Investments, LLC* 129 Cal.
 App.4th 719 (2005). (See Motion to Vacate pp. 7 & 13; Decl. of Ronald P. Kane ¶¶ 25, 26 & 29 .)

830 at 838.) Here, the cases which WFA claims are controlling are not governing law, nor explicit nor clearly applicable. The exact opposite is true. The cases regarding unconscionability, upon which WFA relies, are plainly distinguishable. More egregiously, the one case regarding the litigation privilege, which WFA claims is controlling, is no longer good law.

1. *Koehl v. Verio, Inc. and Federal Savings and Loan Insurance Corp. v. Musacchio* Are Inapplicable.

WFA's argument that the arbitration panel manifestly disregarded the law in ruling that the note was unconscionable is based upon two cases: *Koehl v. Verio, Inc.* 142 Cal. App.4th 1313 (2006) and *Federal Savings and Loan Insurance Corp. v. Musacchio* 695 F. Supp. 1044 (N.D. Cal. 1988). (See Motion to Vacate pp. 7, 8 & 11; Decl. of Ronald P. Kane ¶¶ 25 & 26 .) WFA's reliance upon those cases is misplaced. Neither *Musacchio* nor *Koehl* stand for the proposition that the arbitration panel was required to rule in WFI's favor as a matter of law, irregardless of the facts, circumstances and evidence presented in Mr. Shaffer's case.

Indeed, in *Koehl*, the claim of unconscionability was rejected, not because of the substantive issues, but because it had been waived by the failure to assert it in the lower court. (*Koehl, supra*, 142 Cal. App.4th at 1338.) There was no such waiver here. Mr. Shaffer expressly stated as one of his defenses in his Answer that the note is unconscionable. (Exh. 4.) Further, *Koehl* is factually distinguishable. *Koehl* did not involve a promissory note such as the one at issue here. Instead, it involved a claim by a sales person that commission charge-backs were unconscionable. WFI's claims against Mr. Shaffer involved a promissory note, not commission charge-backs. *Koehl* is plainly inapplicable.

Musacchio is equally inapposite. *Musacchio*, unlike the instant action, did not involve a promissory note drafted by an employer which was signed by the employee, but rather a standard form promissory note executed by a corporate entity who had borrowed money from a bank. The note at issue in *Musacchio* was indisputably an arms-length transaction between two sophisticated entities of equal bargaining power. Equally significantly, *Musacchio* does not hold

1 that no promissory note can ever be unconscionable under California law, regardless of the
 2 circumstances. *Musacchio* simply stands for the unremarkable proposition that standard form
 3 promissory notes are not per se unenforceable. Finally, if *Musacchio* did hold that no promissory
 4 note signed by an employee could ever be deemed to be unconscionable, as WFA insinuates, it
 5 would be at odds with the California Supreme Court's subsequent decision in *Armendariz*, *supra*,
 6 24 Cal.4th 83.

7 WFA also argues that *Banus v. Citigroup Global Markets, Inc.* 2010 U.S. Dist LEXIS
 8 40072, an unpublished case from New York which it did not even cite to the arbitration panel,
 9 somehow shows that the panel manifestly disregarded California law. (Motion to Vacate pp. 11-
 10 12.) WFA provides no explanation as to how the arbitrators could have "manifestly disregarded"
 11 law of which they were never even aware. Equally importantly, *Banus* is an **UNPUBLISHED**
 12 decision from a New York District Court. WFA's claim that the arbitrators manifestly
 13 disregarded California law by failing to follow an unpublished decision from a foreign
 14 jurisdiction is frivolous. Further, WFA has misstated the holding of *Banus*. The *Banus* court
 15 held that the plaintiffs' claims regarding the unconscionability of the note should be dismissed
 16 because all such claims were subject to binding arbitration and must be decided by the
 17 arbitrators. The commentary regarding unconscionability under New York law, that is quoted by
 18 WFA in its motion, is pure dicta.

19 Indeed, *Banus* supports Mr. Shaffer's position that all claims regarding the enforceability
 20 and/or unconscionability of the promissory note were subject to binding arbitration and must be
 21 decided by the arbitrators. That is precisely what occurred here. The arbitrators ruled that the
 22 note was unenforceable because it was unconscionable. As the *Banus* court held, WFA/WFI,
 23 having lost in arbitration, does not have the right to re-litigate its case in a federal district court.

24 **2. *Fontani v. Wells Fargo Investments, LLC* Is Contrary to Subsequent** 25 **California Supreme Court Precedent.**

26 WFA contends that one single California appellate court decision, *Fontani v. Wells Fargo*
 27 *Investments, LLC* 129 Cal. App.4th 719 (2005) conclusively determined that a Form U-5 can
 28

1 never be actionable. (Motion to Vacate pp. 13-14.) That is not an accurate statement of
 2 California law. It is true that the *Fontani* court ruled that the statements made by the broker-
 3 dealer on the Form U-5 at issue in that particular case were protected by the litigation privilege
 4 because they were pre-litigation communications which might lead to a regulatory investigation.
 5 (*Fontani, supra*, 129 Cal. App.4th at 734-736.) However, WFA has omitted to mention that the
 6 California Supreme Court subsequently held, in a decision rendered two years AFTER *Fontani*,
 7 that pre-litigation communications such as statements on a Form U-5 are only protected by the
 8 litigation privilege if they relate to litigation that is contemplated in good faith and under serious
 9 consideration, and that this determination is a fact question. (*Action Apartment, supra*, 41
 10 Cal.4th at 1251-1252.) To the extent that *Fontani* holds otherwise, it is no longer good law. If
 11 the arbitrators' legal reasoning is subject to judicial review - and it is not - it was certainly not
 12 erroneous for them to refuse to apply a California appellate court case which is contrary to
 13 subsequent California Supreme Court precedent.

14 **C. WFA Cannot Meet the Standard for Manifest Disregard for the Law.**

15 WFA's motion would fail, in any event, because there is no evidence that the arbitration
 16 panel manifestly disregarded the law.

17 The Ninth Circuit has made it clear that vacatur of an arbitration award for manifest
 18 disregard of the law is only authorized in extremely narrow and unusual situations. Manifest
 19 disregard of the law means something more than an error in interpreting the law or a failure on
 20 the part of the arbitrators to understand or apply the law. (*Lagstein, supra*, 607 F.3d at 641;
 21 *Bosack, supra*, 586 F.3d at 1104.) A district court may not reverse an arbitration award even in
 22 the face of an erroneous interpretation of the law. (*Collins, supra*, 505 F.3d at 879.) Indeed, the
 23 United States Supreme Court has explicitly rejected the argument that "manifest disregard of the
 24 law" authorizes a district court to review an arbitration award for alleged legal errors. (*Hall*
 25 *Street, supra*, 552 U.S. at 585.) On the contrary, to vacate an arbitration award for manifest
 26 disregard of the law, the moving party must show that the arbitrators understood and correctly
 27 stated the law, but then proceeded to disregard the same. (*Lagstein, supra*, 607 F.3d at 641;
 28

1 *Bosack, supra*, 586 F.3d at 1104; *Collins, supra*, 505 F.3d at 879.) Where, as here, the
2 arbitrators did not explain the legal reasoning behind their award, it is all but impossible to
3 determine that they acted with manifest disregard for the law. (*Bosack, supra*, 586 F.3d at
4 1104.)

5 The Ninth Circuit, applying the foregoing principles, has consistently rejected motions to
6 vacate arbitration awards for alleged manifest disregard for the law, that were nothing more than
7 thinly disguised attempts to revisit the arbitrators' legal and factual conclusions.

8 For example, in *Lagstein, supra*, the Ninth Circuit held that the district court had
9 committed reversible error by vacating an arbitration award for manifest disregard of the law,
10 because there was no evidence of any applicable law that the arbitration panel had explicitly
11 recognized and then ignored. (*Lagstein, supra*, 607 F.3d at 641.)

12 Similarly, in *Bosack, supra*, the party seeking vacatur contended that the arbitration
13 award must be vacated because the arbitrators had allegedly failed to follow California law as
14 described by the petitioner. The Ninth Circuit held that this argument was an improper invitation
15 to review the arbitration panel's factual findings and legal conclusions, and that it was prohibited
16 from doing so under the FAA. (*Bosack, supra*, 586 F.3d at 1104.) The *Bosack* court explained
17 that there was no evidence in the record that the arbitrators understood the law, correctly stated
18 the law, and then proceeded to disregard that law. (*Id.* at 1104-1105.) Consequently, there was
19 no basis for vacating the award for manifest disregard of the law. (*Id.*)

20 Here, as discussed above, the arbitrators properly recognized, cited and applied
21 *Armendariz v. Foundation Health Psychcare Services, Inc.* (2000) 24 Cal.4th 83, which is
22 controlling authority, to the facts and evidence presented in Mr. Shaffer's case. Nonetheless,
23 WFA insists that the arbitrators must have manifestly disregarded the law because WFI provided
24 the arbitrators with copies of the *Koehl, Musacchio* and *Fontani* cases, but the arbitrators still
25 ruled in favor of Mr. Shaffer. WFA's arguments would fail even if *Koehl, Musacchio* and
26 *Fontani* were controlling and clearly applicable (which they are not).

1 First, there is no indication in the award nor in the transcript that the arbitrators explicitly
 2 recognized the *Koehl, Musacchio* and/or *Fontani* cases. Secondly, the award does not cite to the
 3 *Koehl, Musacchio* nor *Fontani* cases. (Exh. 6.) Third, the transcript does not reflect that the
 4 arbitrators cited to the *Koehl, Musacchio* and/or *Fontani* cases. Finally, there is no evidence that
 5 the arbitrators ignored the *Koehl, Musacchio* and/or *Fontani* cases, as opposed to concluding that
 6 they were inapplicable and/or distinguishable. Indeed, where, as here, the arbitration award is
 7 not an explained decision which details the arbitrators' legal reasoning, it would be impossible to
 8 determine that the arbitrators acted with manifest disregard for the law. (See *Bosack, supra*, 586
 9 F.3d at 1104.)

10 At most, the arbitrators failed to apply and/or follow the cases cited by WFI, or
 11 interpreted them differently than WFI. As discussed above, the arbitrators' alleged
 12 misinterpretation of the law, or alleged failure to follow and/or correctly apply the law, would not
 13 be grounds for vacating an arbitration award under the FAA, even if such a misinterpretation or
 14 misapplication had occurred. (*Hall Street, supra*, 552 U.S. at 585-588; *Lagstein, supra*, 607 F.3d
 15 at 641; *Bosack, supra*, 586 F.3d at 1102, 1104; *Kyocera, supra*, 341 F.3d at 994.) WFA must do
 16 more than argue that the arbitrators' legal reasoning and factual findings were erroneous. It has
 17 failed to do so.

18 **VI. WFA WAIVED THE RIGHT TO CLAIM THAT MR. SHAFFER COULD NOT**
 19 **OBTAIN RELIEF FOR THE STATEMENTS MADE IN THE FORM U-5, BY**
 20 **AGREEING TO FINRA ARBITRATION, WHICH EXPLICITLY ALLOWS**
 21 **SUCH CLAIMS.**

22 WFA's predecessor, WFI, selected FINRA as its forum of choice for deciding disputes
 23 with Mr. Shaffer. (Exh. 1, p. 2; Exh. 3.) It expressly agreed, in 2008 and again in 2010, to
 24 abide by FINRA's rules and procedures.⁴ (Exh. 1, p. 2; Exh. 3.) FINRA specifically recognizes
 25 "Libel or Slander on Form U-5" as an employment related dispute which its arbitrators are
 26 empowered to decide. (Exh. 5.) FINRA includes this claim in its list of authorized FINRA

27 ⁴ Although the promissory note included a California choice of law provision, that provision only applies
 28 to the interpretation and enforcement of the Note, not to employment and/or defamation claims which are wholly
 unrelated to the note. (Exh. 1 at p. 2.)

1 claims that are set forth on its Uniform Claim Information Sheet Form, which is available from
 2 the FINRA web-site. (Exh. 5; Shaffer Decl. ¶ 6.) FINRA's rules and procedures plainly allow
 3 for employee claims of libel or slander on a Form U-5, such as the claims made by Mr. Shaffer.

4 Indeed, in *Fahnestock & Co., Inc. v. Waltman* 935 F.2d 512, 515-516 (2nd Cir. 1991), the
 5 Second Circuit Court of Appeals ruled that FINRA arbitrators have the power to decide
 6 defamation claims based on statements in a Form U-5, even if state law privileges bar such
 7 claims. The *Fahnestock* court rejected the very same argument that WFA makes here. (*Id.*)

8 As the *Fahnestock* court recognized, FINRA is entitled to make its own rules, and to hear
 9 claims which might not be allowable if they were to be raised in a state court rather than in
 10 FINRA arbitration. FINRA has determined that securities representatives such as Mr. Shaffer
 11 have the right to arbitrate claims of libel or slander on a Form U-5. WFI selected FINRA as the
 12 forum for hearing and resolving disputes with Mr. Shaffer, and agreed to abide by FINRA's rules
 13 and procedures. By doing so, it waived the right to assert that a state law privilege barred the
 14 FINRA arbitration panel from ruling on the merits of Mr. Shaffer's claims.

15 **VII. WFA'S "PUBLIC POLICY" ARGUMENT IS NOT A VALID GROUNDS FOR** 16 **VACATING THE AWARD.**

17 WFA also asserts that the award must be vacated based upon alleged "public policy"
 18 considerations. WFA's argument is contrary to the express language of Section 10 of the FAA,
 19 and the United States Supreme Court's decision in *Hall Street, supra*. Further, WFA has grossly
 20 misconstrued the one Ninth Circuit case upon which it relies.

21 As discussed above, the ONLY grounds for vacating an arbitration award are the grounds
 22 set forth in Section 10 of the FAA. (*Hall Street, supra*, 552 U.S. at 584-585.) An alleged
 23 violation of public policy is not one of those grounds. (9 U.S.C. § 10.)

24 *Stead Motors of Walnut Creek v. Automotive Machinists Lode No. 1173* 886 F.2d 1200
 25 (9th Cir. 1989), the sole case cited by WFA in support of its argument, is inapposite. First, *Stead*
 26 *Motors* was not brought under the FAA, but rather under the National Labor Relations Act. The
 27 court's opinion expressly concerned the appropriate standard of judicial review for labor
 28

1 arbitration awards. The instant action does not concern a labor arbitration award decided under
2 the National Labor Relations Act. *Stead Motors* is plainly inapplicable.

3 Secondly, *Stead Motors* pre-dates the United States Supreme Court's decision in *Hall*
4 *Street, supra*, which held that federal courts cannot make exceptions to the limited scope of
5 judicial review set forth in Section 10 of the FAA. To the extent that *Stead Motors* may be
6 construed as holding that an alleged violation of public policy is a separate grounds for vacatur
7 under the FAA, it is contrary to United States Supreme Court precedent.

8 Third, WFA misstates the holding of *Stead Motors*. Specifically, the *Stead Motors* court
9 held that the "public policy exception" to judicial review of labor arbitration awards is limited to
10 situations where the enforcement of an arbitration award and/or the underlying contract giving
11 rise to the award would force a party to perform a manifestly illegal act. (*Stead Motors, supra*,
12 886 F.2d at 1211-1213, 1216-1217.) Indeed, the *Stead Motors* court reversed the district court's
13 order, which had vacated the arbitration award on public policy grounds. The *Stead Motors*
14 court expressly cautioned against allowing the public policy exception to "be turned into a facile
15 method of substituting judicial for arbitral judgment". (*Id.* at 1212.) As the Ninth Circuit has
16 subsequently explained, mere inconsistency with a court's generalized view of public policy is
17 not an appropriate ground for vacatur of an arbitration award. (*Lagstein, supra*, 607 F.3d at 641,
18 fn. 4.)

19 As the authorities above hold, WFA is not entitled to vacate the award merely because it
20 is allegedly inconsistent with WFA's view of public policy. If the public policy exception
21 applies at all to proceedings brought under the FAA, then WFA must show that enforcing the
22 award would require WFA to do something that is illegal. WFA has made no such showing.
23 There is nothing illegal about requiring an entity to pay damages to an individual. Similarly,
24 holding WFA to its predecessor's own arbitration agreements is neither illegal nor a violation of
25 public policy. Indeed, vacatur of the award based upon alleged public policy considerations
26 would be contrary to the public policy that supports the enforceability of arbitration agreements
27 and the finality of arbitration awards.

VIII. MR. SHAFFER SHOULD BE AWARDED HIS ATTORNEYS FEES INCURRED IN OPPOSING THIS MOTION, PURSUANT TO THE TERMS OF THE NOTE.

A prevailing party is entitled to an award of the attorneys fees incurred in litigating a petition to vacate an arbitration award, if the agreement between the parties provides for attorneys fees. (*A.G. Edwards & Sons, Inc. v. McCollough*, 967 F.2d 1401, 1404 (9th Cir. 1992).)

Such is the case here. The promissory note between the parties contains a one-sided provision for attorneys fees to be awarded to WFI in the event that any action or lawsuit is required to be brought for the collection of any amount under the note, including all fees involved in collection. (Exh. 1, p. 2.) The note further provides that it shall be interpreted, enforced and governed by California law. (Exh. 1, p. 2) Pursuant to California Civil Code § 1717, the one-sided provision for attorneys fees in the note must be made reciprocal. Consequently, Mr. Shaffer is entitled by contract and by law to recover the attorneys fees he has incurred in defending WFA's efforts to collect on the note. This necessarily includes the fees incurred in defending the instant motion to vacate the arbitration award which held the note to be unconscionable.

IX. CONCLUSION

For the foregoing reasons and authorities, respondent Kenneth C. Shaffer respectfully requests this honorable court deny WFA's motion to vacate the arbitration award issued in the *Matter of the Arbitration Between Wells Fargo Investments, LLC and Kenneth C. Shaffer*, FINRA Case No. 10-00773. Mr. Shaffer further respectfully requests this honorable court award him his attorneys fees incurred in opposing the instant motion to vacate, in an amount to be determined pursuant to motion at the appropriate time.

Dated: May 18, 2011

STANZLER LAW GROUP

By: Melinda Steuer
Melinda Jane Steuer
Attorneys for Respondent Kenneth C. Shaffer

PROOF OF SERVICE

[C.C.P. § 1013, C.R.C. § 2008, F.R.C.P. Rule 5]

I, Sharran L. Rodd, state:

I am a citizen of the United States. My business address is 2275 E. Bayshore Rd., Suite 100, Palo Alto, CA 94303. I am employed in the City of Palo Alto, County of Santa Clara where this mailing occurs. I am over the age of eighteen years and not a party to this action. On the date set forth below, I served the foregoing documents described as:

MEMORANDUM OF POINTS AND AUTHORITIES IN OPPOSITION TO WELLS FARGO ADVISORS, LLC'S MOTION TO VACATE ARBITRATION AWARD

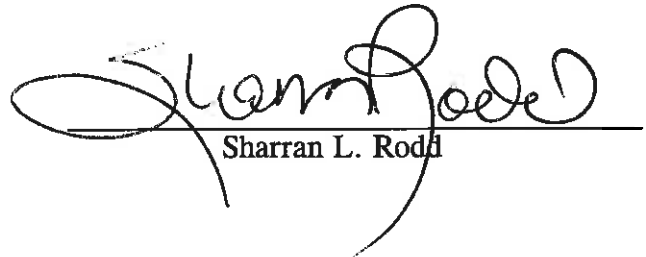
on the following person(s) in this action via ECF addressed as follows:

Fredrick A. Rafeedie, Esq.
Samuel E. Endicott, Esq.
Jones, Bell, Abbott, Fleming & Fitzgerald LLP
601 South Figueroa Street, 27th Floor
Los Angeles, CA 90017-5759

X: Filed and Served electronically in accordance with the Court's electronic filing ("ECF") rules, pursuant to which registered ECF users receive service copies by e-mail delivery.

I declare under penalty of perjury under the laws of the State of California that the foregoing is true and correct and that this declaration was executed this date at Palo Alto, California.

Dated: May 19, 2011



Sharran L. Rodd